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May 28, 2013

GLORIA L. FRANKLIN, CLERK
U.S. BANKRUPTCY COURT
NORTHERN DISTRICT OF CALIFORNIA

Signed and Filed: May 27, 2013



Dennis Montali

DENNIS MONTALI
U.S. Bankruptcy Judge

UNITED STATES BANKRUPTCY COURT

NORTHERN DISTRICT OF CALIFORNIA

In re) Bankruptcy Case
) No. 13-30340DM
GABRIEL TECHNOLOGIES CORP., et al.,) (No. 13-30341)
)
Debtors.) Chapter 11
)

MEMORANDUM DECISION ON MOTION FOR CONVERSION TO
CHAPTER 7 OR APPOINTMENT OF A CHAPTER 11 TRUSTEE

I. INTRODUCTION

On April 3, 2013, Qualcomm Incorporated ("Qualcomm") filed a Motion By Qualcomm Incorporated, Pursuant To 11 U.S.C. § 1112 For Conversion To Cases Under Chapter 7 Or, In The Alternative, For Appointment Of A Chapter 11 Trustee, For Cause (the "Motion") (Docket No. 40). Debtors, Gabriel Technologies Corporation and Trace Technologies LLC ("Debtors"), opposed the Motion. The Official Committee of Unsecured Creditors ("Committee") filed a Statement Of Position opposing the Motion. The matter was fully briefed and argued before the court on May 17, 2013.

For the reasons explained below, the court will deny the Motion.

1 II. DISCUSSION¹

2 On February 1, 2013, the United States District Court for the
3 Southern District of California, in an action there by Debtors
4 against Qualcomm and other defendants for misappropriation of
5 intellectual property and related patent disputes (the "District
6 Court Action"), entered an order directing Debtors to pay Qualcomm
7 and the two other parties nearly \$12-1/2 million in attorneys'
8 fees; after credit of an \$800,000 bond that had been posted in
9 Qualcomm's favor, Debtors were ordered to pay the remaining amount
10 of over \$11-1/2 million. That outcome and a judgment in favor of
11 Qualcomm was the culmination in the District Court Action of
12 expensive and extensive litigation initiated in 2008. Debtors are
13 appealing that adverse judgment and the attorneys' fees award and
14 stake their future in this Chapter 11 case on a successful appeal
15 and thereafter a trial or some other favorable disposition. They
16 were unable to obtain a bond to stay Qualcomm's enforcement of the
17 attorneys' fees award although exactly what assets Qualcomm could
18 reach is not evident.

19 When Debtors filed these Chapter 11 cases on February 14,
20 2013, they had ceased all business operations, had no employees,
21 no customers, no products, and no source of operating income. The
22 schedules show tangible assets (office furniture) valued at \$200,
23 cash of less than \$300 and a \$1500 lease deposit. What remains of
24 any hope of a claim against Qualcomm has an unknown value and
25 there is no mention of the potential claim against officers and
26 directors mentioned below.

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28 ¹ The following discussion constitutes the court's findings
 of fact and conclusions of law. Fed. R. Bankr. P. 7052(a).

1 The Motion, in short, urges that an independent trustee be
2 appointed under either Chapter 7 or Chapter 11, so that the
3 trustee may make an objective assessment of whether and if to
4 continue to prosecute the appeal against Qualcomm, and whether and
5 if to prosecute an action against former officers and directors of
6 Debtors for initiating and unsuccessfully prosecuting the District
7 Court Action. Qualcomm also has spent a great deal of time in its
8 papers supporting the Motion to be highly critical of prior
9 management of the Debtors, and to stress that the current
10 management, along with the members of the Committee, are
11 irreconcilably conflicted and should not be permitted to dictate
12 the outcome of these Chapter 11 cases.

13 Debtors believe that they should remain in possession and be
14 given an opportunity to seek confirmation of a Chapter 11 plan.
15 To that end, on April 24, 2013, they filed Debtors' Joint Plan Of
16 Reorganization (April 24, 2013) (the "Plan"), together with a
17 draft [proposed] Disclosure Statement for the Plan. Qualcomm
18 contends that the Plan is patently unconfirmable; Debtors and the
19 Committee disagree. For purposes of ruling on the Motion, the
20 court makes no determination on whether the Plan, or any variation
21 of it, could be confirmed.² That will come later.

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25 ² At the hearing on May 17, the court asked the Debtors'
26 counsel about the possibility of deferring any consideration of
27 the Plan while they prosecute their appeal. That suggestion was
28 rejected, in part, because the Debtors believe they can obtain
funding from a third party who desires confirmation of the Plan
and is apparently willing to provide some sort financing to
facilitate that outcome.

1 The Motion was brought under § 1112(b).³ That subsection
2 provides, in part:

3 **(b)(1)** Except as provided in paragraph (2) and
4 subsection (c), on request of a party in interest, and
5 after notice and a hearing, the court shall convert a
6 case under this chapter to a case under chapter 7 or
7 dismiss a case under this chapter, whichever is in the
best interests of creditors and the estate, for cause
unless the court determines that the appointment under
section 1104(a) of a trustee or an examiner is in the
best interests of creditors and the estate.

8 **(2)** The court may not convert a case under this chapter
9 to a case under chapter 7 or dismiss a case under this
10 chapter if the court finds and specifically identifies
11 unusual circumstances establishing that converting or
dismissing the case is not in the best interests of
creditors and the estate, and the debtor or any other
party in interest establishes that--

12 **(A)** there is a reasonable likelihood that a plan will be
13 confirmed within the timeframes established in sections
14 1121(e) and 1129(e) of this title, or if such sections
do not apply, within a reasonable period of time; and

15 **(B)** the grounds for converting or dismissing the case
16 include an act or omission of the debtor other than
under paragraph (4)(A)--

17 **(i)** for which there exists a reasonable justification for the
act or omission; and
18 **(ii)** that will be cured within a reasonable period of time
fixed by the court.

19 * * *

20 **(4)** For purposes of this subsection, the term 'cause'
includes--

21 **(A)** substantial or continuing loss to or diminution of
the estate and the absence of a reasonable likelihood of
22 rehabilitation;

23 **(B)** gross mismanagement of the estate;

24 11 U.S.C. § 1112.

25 Qualcomm did not base the Motion on § 1104(a), which permits

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27 ³ Unless otherwise indicated, all chapter, section and rule
references are to the Bankruptcy Code, 11 U.S.C. §§ 101-1532, and
28 to the Federal Rules of Bankruptcy Procedure, Rules 1001-9037.

1 an appointment of Chapter 11 trustee or an examiner but does not
2 deal with dismissal or conversion.

3 Conversion or dismissal is available under § 1112(b)(1) "for
4 cause". The burden is on the moving party (Qualcomm) to establish
5 cause. 7 COLLIER ON BANKRUPTCY, ¶ 1112.04 [4] (Henry Sommers & Alan
6 Resnick, 16th ed. 2009). "Thus, until the movant carries this
7 burden, the statutory direction that the court 'shall convert the
8 case to a case under chapter 7 or dismiss the case' is not
9 operative." *Id.*

10 Section 1112(b)(4) enumerates sixteen different and
11 nonexclusive illustrations of cause. For purposes of this Motion,
12 the only two of those sixteen alternatives urged by Qualcomm are
13 found in § 1112(b)(4)(A), "substantial or continuing loss to or
14 diminution of the estate and the absence of a reasonable
15 likelihood of rehabilitation" and § 1112(b)(4)(B), "gross
16 mismanagement of the estate." Qualcomm has not carried its
17 burden of establishing cause under either alternative.

18 Because the debtor has no tangible assets or realizable value
19 and no operations, there has not been and is no "substantial" loss
20 or diminution of the estate. Simply stated, there is nothing left
21 to lose. The question then becomes whether accrual of fees of
22 professionals employed by the Debtors and the Committee, and the
23 possibility of additional Delaware state taxes, amount to the type
24 of "continuing loss" that Congress had in mind to trigger the
25 nearly mandatory conversion, dismissal or chapter 11 trustee
26 options § 1112(b)(1) contemplates.

27 Perhaps from an accounting perspective (profit and loss),
28 such accruals would constitute such losses. But the accrual of

1 liabilities are not the same as the incurring of actual out-of-
2 pocket losses, such as the dissipation of assets that diminishes
3 the estate. Leaving the Debtors in possession of the chapter 11
4 estate is not risking some ever-diminishing pool of assets.⁴

5 Even if that were the case, the court must consider how long
6 a situation must persist to be said to be continuing for purposes
7 of § 1112(b)(4)(A). These jointly administered cases are just
8 over three months along and the Debtors have already filed the
9 Plan that will be tested very soon. The accrual of liabilities
10 (losses) will end soon, either with a confirmed joint plan or
11 conversion to chapter 7, a point conceded by Debtors' counsel to
12 be inevitable if confirmation is denied. Thus, even if there is
13 any continuing loss at all, it will not be continuing very long at
14 all.

15 Because § 1112(b)(4)(A) uses the conjunctive (loss and
16 absence of likelihood of rehabilitation) the court does not need
17 to deal with the thorny question of whether "absence of a
18 reasonable likelihood of rehabilitation" applies to debtors whose
19 only hope is a successful appeal of an adverse litigation result
20 and retrial, and has no going concern or business to rehabilitate.

21 The only other "cause" trigger under § 1112(b)(4) is the
22 gross mismanagement of the estate under § 1112(b)(4)(B). Qualcomm
23 is long on rhetoric about the potential conflicts that it believes
24 infect current management but it has not provided any proof of

25 ⁴ One court has even suggested that where the debtor is not
26 an operating company, but merely holds an intangible asset, the
27 loss - diminution factor is not even relevant. In re 3 Ram, Inc.,
28 343 B.R. 113, n. 14 (Bankr. E.D. Pa. 2006) (but case dismissed
because proposed plan was not feasible and feasible plan not
possible).

1 specific mismanagement in the short time Debtors have been in
2 control of the estate. It has not established cause under that
3 alternative.

The Plan, or some variation of it, may or may not be confirmable, and Debtors and the Committee will have to deal with anticipated objections to confirmation that Qualcomm will likely make. That is for another day. On the face of it, the court cannot say that the Plan is unconfirmable as a matter of law.

What the court can say, however, is that if Debtors do not obtain confirmation within the timetable to be set, Qualcomm will have its wish, albeit under § 1112(b)(4)(J) ("failure to file a disclosure statement, or to file or confirm a plan, within the time fixed ... by order of the court;").

14 || III. CONCLUSION

15 For the foregoing reasons, the court will deny the Motion by
16 a separate order being issued concurrently with this Memorandum
17 Decision. The court will conduct a Status Conference on June 10,
18 2013, at 1:30 p.m., at which time it will set a tight schedule for
19 consideration of a final disclosure statement to accompany either
20 the Plan or any revised plan Debtors may file before then.
21 Debtors' counsel is directed to meet and confer with the
22 Committee's counsel and with Qualcomm's counsel to discuss any
23 necessary discovery prior to consideration of the disclosure
24 statement and further to discuss a time table for a hearing on
25 approval of the final disclosure statement and confirmation of the
26 Plan or any other plan that may be filed. The court expects those
27 hearings to be concluded by the end of August, 2013.

END OF MEMORANDUM DECISION

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